

# Serving the Nation – Through Effective Financial Management

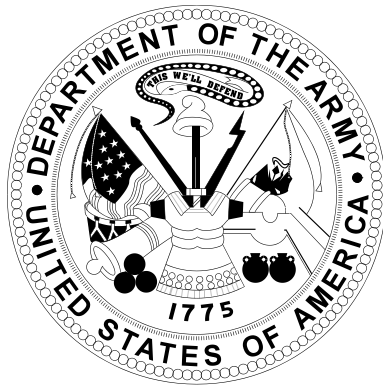
FY 1994 Financial Activity



March 1995

***"Improved Army financial management, accountability, and stewardship is everyone's responsibility. It is a journey, not a destination."***

***—General Gordon R. Sullivan, Chief of Staff of the Army***





## **Objectives**

This document is designed to provide the users of the Army's financial report with an understanding of key decision-making information from the financial management process and related legislative requirements. It focuses on financial information from the Army's Fiscal Year 1994 audited financial statements, required by the Chief Financial Officers Act of 1990. The document relates this information to current and future financial management initiatives.

## Organization of the Guide

***Section I — Improving Financial Management*** — discusses recent legislative initiatives that are designed to improve financial management, and focuses on the Army's implementation of the Chief Financial Officers Act.

***Section II — Future Challenges*** — identifies how resource challenges are affecting the Army's functional areas, and emphasizes the importance of improving financial management to meet these challenges.

***Section III — 1994 Audited Financial Statements*** — discusses the 1994 Financial Statements and related Audit Reports.

***Section IV — Other Financial Management Initiatives*** — presents additional financial issues of which functional managers should be aware.

***Section V — Continuing Process Improvements*** — provides a synopsis of ongoing and future financial management initiatives.

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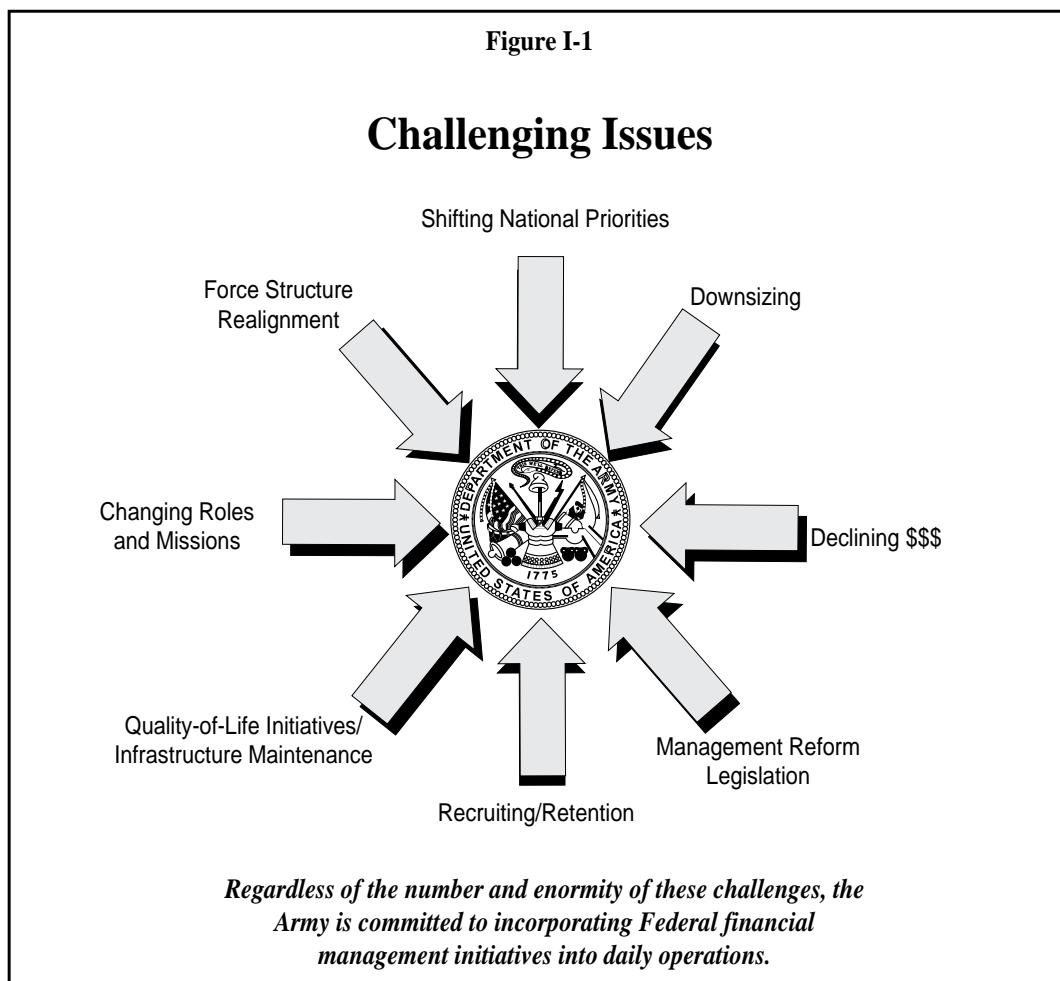
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## I. Improving Financial Management

As the 21st century nears, increasing management demands and a dynamically changing global environment are creating unprecedented challenges and opportunities for the United States Army (the Army). Decreasing resources and new management reform legislation are changing the financial management landscape.

Army managers must consider the new global environment when responding to programs and financial management challenges into the 21st century, as shown in Figure I-1.





### Management Reform Legislation

Within the Federal government, there is broad acceptance of the need to improve stewardship by managing resources more effectively and becoming more accountable to the taxpayers. In response, Congress has enacted three important legislative

***"It is up to each of us to ensure that Army stewardship is, and is perceived to be, above reproach."***

— General Gordon R. Sullivan, Chief of Staff of the Army

initiatives during the past five years that focus on improving management in the Federal government: the Chief Financial Officers (CFO Act) of 1990, the Government Performance and Results Act (GPRA) of 1993, and the Government Management Reform Act (GMRA) of 1994. These initiatives are summarized in Figure I-2.

The CFO Act provides a framework for continuous improvement of financial management, which is done by improving stewardship of resources and

***"The real value of our efforts to implement the CFO Act has been the analysis and modification of functional processes to improve them and meet financial management requirements."***

— Ms. Helen T. McCoy, Assistant Secretary of the Army (Financial Management and Comptroller), Testimony before the Senate Committee on Governmental Affairs, July 1994

accountability to the taxpayers. These changes will help the Army to utilize resources more effectively and to integrate program and financial management.

The Army must continue to increase data integrity, enhance horizontal communication of information, and improve functional processes on which it bases operational and functional decisions. Establishing an improved interrelationship among sound financial management practices, the availability of quality information on which to base decisions, and operational readiness is imperative.

Financial Management Reform Legislation Affecting the Army
<p><u>The CFO Act</u></p> <p>Requirements and Purpose</p> <ul style="list-style-type: none"> <li>• Requires agencies to develop financial statements that are subject to an audit.</li> <li>• Requires agencies to develop Annual Financial Reports.</li> <li>• Provides a framework to assess financial management "health."</li> <li>• Focuses on stewardship throughout the functional and financial communities.</li> <li>• Promotes horizontal communication between the functional and financial communities.</li> </ul> <p>Army Implementation Status</p> <ul style="list-style-type: none"> <li>• As a CFO Pilot agency, the Army developed its first audited financial statements for Fiscal Year (FY) 1991. FY 1994 is the fourth consecutive year of developing financial statements and undergoing an audit.</li> </ul>
<p><u>GPRA</u></p> <p>Requirements and Purpose</p> <ul style="list-style-type: none"> <li>• Requires agencies to develop strategic plans and annual plans with program performance goals.</li> <li>• Requires agencies to submit annual reports to measure actual program performance against planned goals and objectives.</li> <li>• Improves internal management and program effectiveness by systematically holding agencies accountable for results.</li> </ul> <p>Army Implementation Status</p> <ul style="list-style-type: none"> <li>• The Army currently is developing an implementation plan. Three organizations within the Army are pilots. Full implementation is planned for FY 1999.</li> </ul>
<p><u>GMRA</u></p> <p>Requirements and Purpose</p> <ul style="list-style-type: none"> <li>• Expands the financial statements requirements of the CFO Act to include all activities of the 24 Executive Branch agencies covered by the CFO Act. These agencies must develop agency-wide financial statements for FY 1996.</li> </ul> <p>Army Implementation Status</p> <ul style="list-style-type: none"> <li>• The Army has a head start, having been a pilot for CFO Act implementation. The Army will experience consolidation issues related to the DoD Department-wide statements, which must be developed by FY 1996.</li> </ul>

Figure I-2

### **The Army, a Leader in CFO Act Implementation**

***"...the Department of the Army has demonstrated proactive involvement from top management officials in resolving problems disclosed by the audits."***

— Mr. Charles A. Bowshe, Comptroller General of the United States,  
Testimony before the Senate Committee on Governmental Affairs, July  
1994

The Army has been recognized by the General Accounting Office (GAO) and the regulatory community as a leader in CFO Act implementation, based on its progress since 1991 when the Army was designated a CFO Pilot organization.

<b><i>Audited financial statements serve as both a tool for internal financial management and a vehicle for demonstrating accountability to the public.</i></b>	The Army has been proactive as a CFO Act Pilot organization. It has prepared financial statements and has been responding to audit findings for four consecutive years. Senior leaders have communicated the message that stewardship is the responsibility of everyone throughout the organization. These leaders have encouraged horizontal communication between functional and financial communities.
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Among the key provisions of the CFO Act is a requirement for Federal agencies to produce audited financial statements for certain activities.

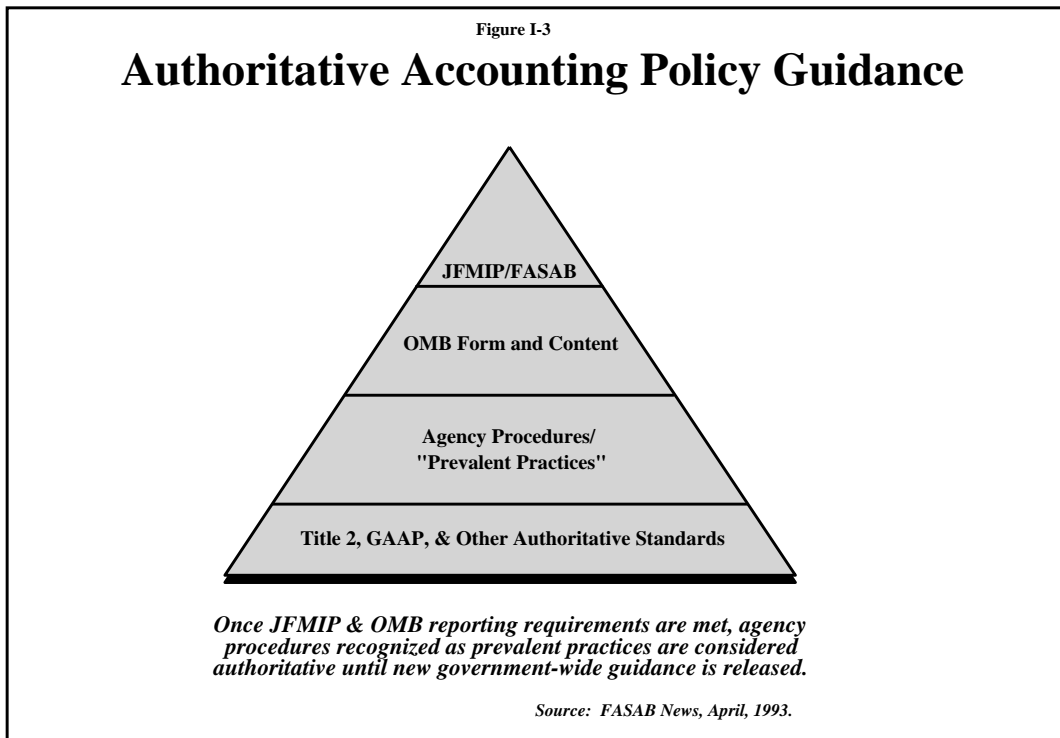
Financial statements provide a historical look at an entity's financial position and results of operations. They are not an end in themselves. Much of the benefit of financial statements comes in coordinating the people, systems, functional processes, and financial information required to prepare them. The requirement to prepare financial statements forces discipline and systemic improvement on the entire

entity. Because financial statements are required annually, improvement is continuous.

Financial statements are prepared based on a hierarchy of standards. The top of the hierarchy is individual accounting standards proposed by the Federal Accounting Standards Advisory Board (FASAB) and published by the Joint Financial Management Improvement Program (JFMIP) principals — the Office of Management and Budget (OMB), the GAO, and the Department of the Treasury. The second level of the hierarchy is guidance, issued by OMB, on the form and content of financial statements. To the extent that authoritative guidance is not available from FASAB and OMB, agencies are allowed to follow internal accounting policies and procedures provided they are “prevalent practices” throughout the Federal government. In the absence of specific policy as dictated above, agencies may follow accounting standards published by other authoritative bodies, e.g., Policy and Procedures Manual for Guidance of Federal Agencies Title 2 (Title 2) Accounting, and generally accepted accounting principles (GAAP).

The hierarchy shown in Figure I-3 presents the authoritative rank of each standard-setting body.

Financial statement audits also are required annually, in accordance with prescribed procedures. The scope of the audit encompasses the financial statements and addresses related internal controls and compliance with applicable laws and regulations. Financial statement audits force discipline on the financial management process because auditors address the same areas every year and report on the progress made in correcting previously identified findings.



The Army is striving to make CFO Act implementation seamless for functional and financial managers throughout the organization. Two examples of areas where the Army is emphasizing CFO Act concepts are in the design of Force XXI and the Stewardship Task Force.

### ***Information-Based Force — Force XXI***

The FY 1996 *Statement on the Posture of the United States Army* envisions an information-age force that continues to overmatch our adversaries

***"In this new Army, information will be almost as important as ammunition."***

— *The Hon. Togo D. West, Jr., Secretary of the Army*

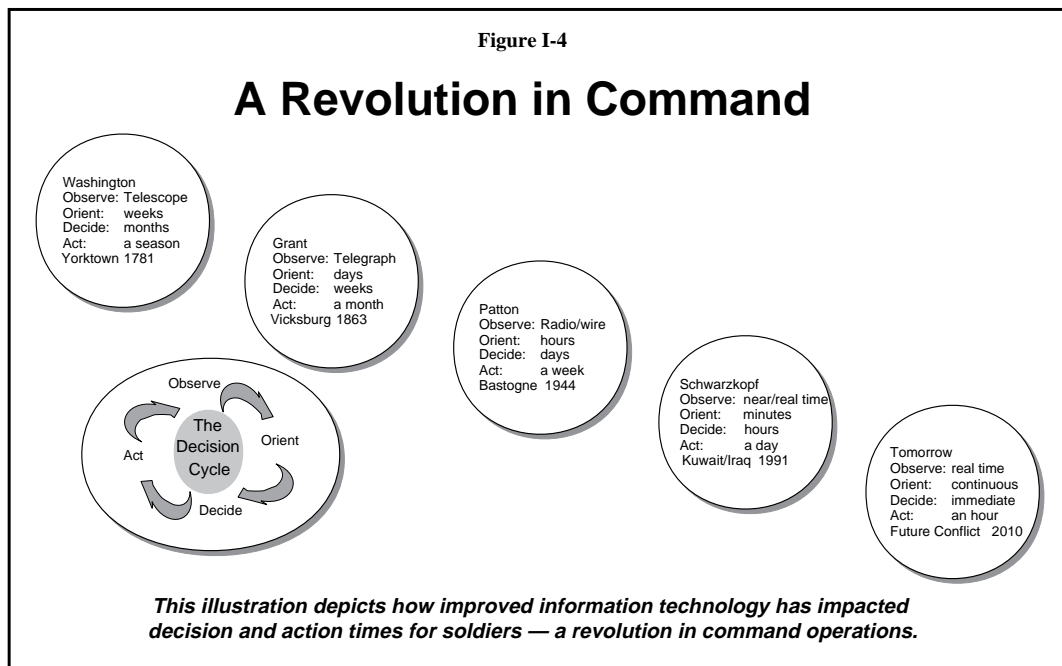
technologically and minimize risks to our soldiers with the most accurate information in the most effective manner. This Army of the 21st century will be called Force XXI. Force XXI focuses on connectivity — how the Army puts the force together when

the information-age force is in place. Information throughout the Army is critical to the successful implementation of Force XXI.

The Army has launched several recent initiatives — the Louisiana Maneuvers, Battle Labs, and General Headquarters Exercises — that are designed to help move the Army from an industrial age to an information age.

*The Army's functional areas must be supported by a strong financial infrastructure with accurate financial information and effective functional processes.*

As the need grows for quality information in support of Force XXI, the need for everyone in the Army to understand and help implement information-age requirements becomes critical. Figure I-4 illustrates how improving information technology over 200 years has led to faster response times. Sound financial information will be essential in achieving an effective Force XXI. Stewardship and accountability must be improved and correlated with force redesign.



### *Stewardship Task Force (vision, goals, objectives)*

Improving stewardship and accountability requires a top-priority, organization-wide focus using effective tools for problem identification, resolution, and monitoring. To provide the top priority focus, the Army established the Senior Level Steering Group (SLSG) composed of top managers from each of the Army's functional areas.

***“Management controls are means to two fundamental ends: mission accomplishment and stewardship for our customers — the American people.”***

*— Joe R. Reeder, Under Secretary of the Army*

The SLSG is defining a Stewardship Improvement Plan (SIP), a comprehensive plan to achieve an “operating end state” for improved financial management and stewardship. The group is focusing on ways the Army does business at several operating levels by re-engineering business practices, strengthening communication, and going beyond correcting problems identified in the Army's financial statement audits.

A proposed vision statement for the SIP reads:

“America's Army...Responsible stewards at every level in the organization and accountable to the people we serve — the American public.”

The SLSG chartered subgroups to support implementation of the SIP. The three subgroups focus on various issues related to improved stewardship of resources, e.g., financial management, logistics, facilities, systems, process improvements.

A sample SLSG initiative from the plan decision briefing in October 1994 is presented in Figure I-5.

A number of similar initiatives are being developed and implemented. This formal process for improving stewardship and accountability directly supports the Army's vision

for Force XXI. It exemplifies the integration of program and financial management that is so important in today's operating environment.

### **Figure I-5**

#### **Sample SIP Initiative**

Title: Army National Guard Unit Cost Analysis System

Description: A customer-oriented, Inter-service Support Agreement (ISA) system that includes a cost database, methodologies to identify and measure direct and indirect costs, and algorithms that allocate overhead costs to the appropriate mission cost center.

Goal Supported: Improve business practices within the Army.

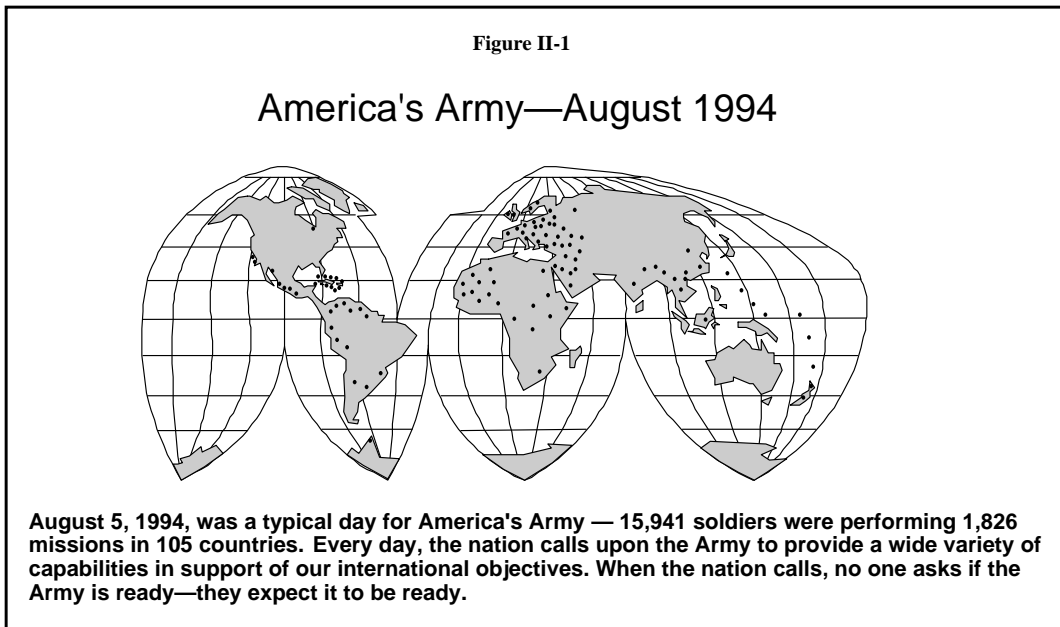
Objectives:

- Increase efficiency by initiating commercial-like business practices that allow greater flexibility in selecting "best value" sources of installation support.
- Compete as a provider of base support services and, within market dynamics, recover the full cost of providing support.



## II. Future Challenges

In FY 1994, thousands of soldiers were operationally deployed to more than 70 countries on any given day. Figure II-1 illustrates the locations of the Army's missions for one day during 1994.



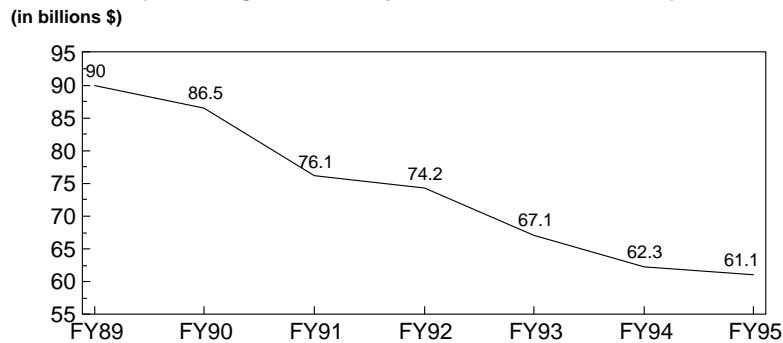
The Army continues to be the "Force of Choice" for deterring aggression and providing a quick response in times of natural disasters. However, decreasing financial resources, as shown in Figure II-2, are forcing the Army to consider trade-offs in day-to-day operations.

The Army's FY 1995 Posture Statement, *Challenges and Opportunities*, discussed how resource challenges are affecting the Army's functional areas. The FY 1996 Posture Statement expands on the resource challenges while describing opportunities in the Army's transformation to an information-age organization.

Figure II-2

## Army Dollar Resource Trends

(Total Obligation Authority in FY 1995 Constant Dollars)



*The Army's buying power has decreased more than 32 percent over a seven-year period.*

The theme of the FY 1996 Posture Statement is "Serving the Nation." The posture statement describes how the Army must transform itself into an organization that has changed the way it thinks, operates, and conducts business. Financial management issues from the Posture Statement are summarized in the remainder of this section as they are related to Budget Resources, Personnel Resources, Logistics, Infrastructure and Installations. These future challenges as identified in the FY 1996 Posture Statement must be considered by functional managers in reviewing the results of 1994 financial activities presented in Section III.

### Budget Resources

The Army's resource challenges are summarized in Figure II-3.

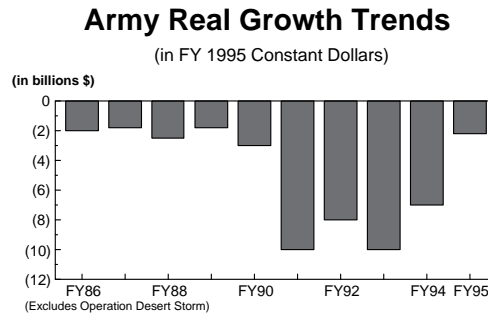
*The Army has experienced a three-fold increase in missions abroad since 1989.*

Although missions are increasing, the real buying power of the Army's budget resources has

Figure II-3

## Resource Challenges

- The Army often must finance and execute unfunded contingency operations.
- The Army must prepare for and fund Force XXI while maintaining readiness and quality-of-life initiatives in the present.
- The Army budget has decreased in constant dollars for 10 consecutive years.
- The Army must be perceived as a model steward of taxpayer funds.



*The Army budget has decreased in constant dollars for 10 consecutive years.*

decreased for the 10th consecutive year. Decreasing resources are forcing the Army to make difficult decisions regarding funding for operations versus readiness.

The Army received supplemental appropriations to cover the costs of unplanned missions for 1994; the additional funding, however, was not sufficient to cover all of the costs. In response, the Army has had to divert Operations and Maintenance (O&M) budget resources from readiness programs to fund the shortfalls. Figure II-4 summarizes these missions and the funding that was directed from readiness programs.

FY 1994 Contingency Operations			
(in Millions)			
Contingency	Funding Required	Funding Provided	Funding Shortfall
Somalia	\$320.4	\$305.0	(\$15.4)
S.W. Asia	70.8	67.0	(3.8)
Yugoslavia	49.6	48.1	(1.5)
Korea	44.8	0.0	(44.8)
Rwanda	30.8	0.0	(30.8)
Haiti	13.4	4.0	(9.4)
Other	14.3	0.0	(14.3)
Total	\$544.1	\$424.1	(\$120.0)

Figure II-4

Funding trade-offs are constraining readiness capabilities. The Army's 1994 Annual Financial Report (AFR) emphasized that:

"The Army has met the resource challenge successfully to date by delaying or deferring modernization and investment, a strategy that has largely run its course. This strategy cannot be further exploited without mortgaging the future." The report explained that the diversion of these resources resulted in:

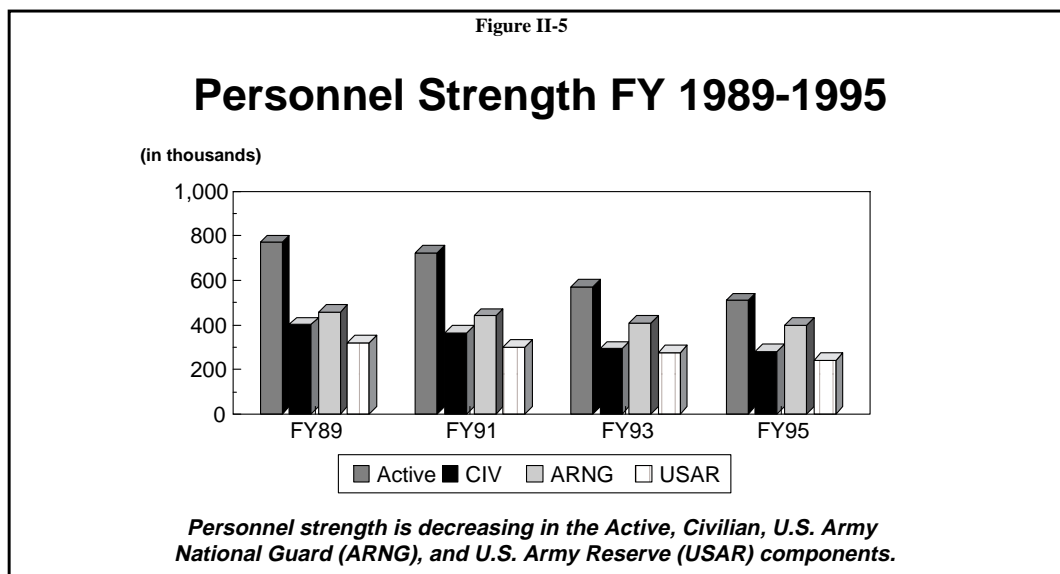
- reduction or cancellation of unit training,
- termination of certain training courses,
- reduction of vehicle maintenance,
- restriction of spare parts purchases, and
- deferral of real property maintenance projects.

***"Three Army divisions lack the readiness to perform all wartime missions. This is the first time in twelve years that the Army has had as many as three divisions rated in this category."***

*Pentagon announcement,  
November 1994*

## Personnel Resources

Personnel strengths, both military and civilian, have been declining since 1989, as shown in Figure II-5.



By the end of FY 1995, the active component strength will be reduced to 510,000 soldiers — a planned reduction of 30,000 soldiers from the FY 1994 end strength. Likewise, the civilian work force will decline from 293,500 at the end of FY 1994 to 281,000 by the end of FY 1995.

Challenges related to the reduction in personnel are summarized in Figure II-6.

Figure II-6

## Personnel Challenges

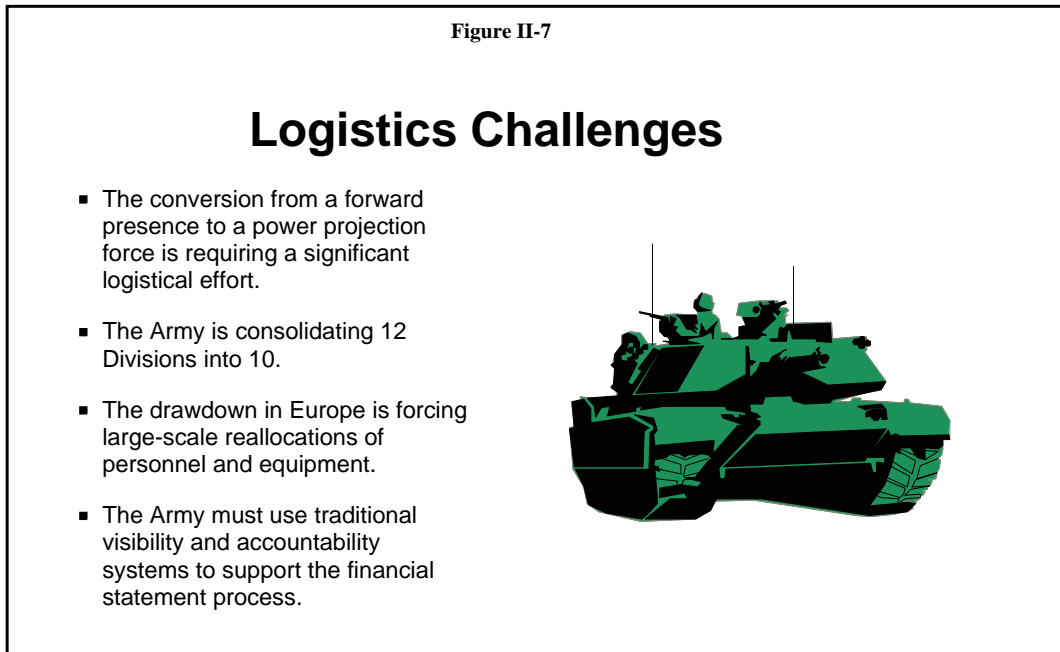
- As the Army draws down its military and civilian forces, institutional knowledge and experience must not be sacrificed.
- Fewer personnel and increasing numbers and types of missions require additional training to ensure quality and consistent work products.
- As the Army nears its end state from the drawdown, accession and retention goals will increase.
- The Army must offer sufficient quality-of-life incentives to continue to be an employer of choice for the best and brightest in an increasingly competitive job market.



## Logistics

The overall downsizing of the Army, in particular the European drawdown and Base Realignments and Closures, is creating significant logistics challenges for the Army. Other challenges are the redistribution of equipment and personnel to meet Force Structure changes as the Army consolidates its 12 Active Army divisions into 10 divisions during FY 1995. The Army will save resources over the long term as these changes are successfully implemented. However, in the short term these

changes require a substantial cash outlay that further squeezes the shrinking Army budget. Logistics challenges are summarized in Figure II-7.



### Infrastructure and Installations

The combined effects of personnel downsizing, force structure realignments, transformation to a power projection force, and diversion of funds to cover unplanned contingency operations place tremendous demands on the Army's infrastructure and installations. These challenges are summarized in Figure II-8.

The Army's Continental United States (CONUS) facilities are adapting to changing conditions and challenges; however, installations are aging and showing further deterioration. The Army has introduced quality-of-life programs, such as the Whole

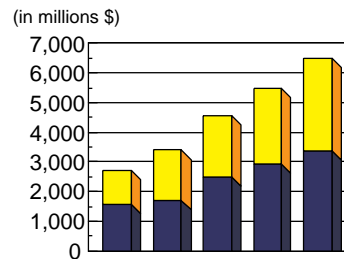
*With stable or decreasing funding, the Army must continually weigh trade-offs between modernization and improving training and living conditions for today's soldiers.*

Figure II-8

## Installation Challenges

Backlog of Maintenance and Repair (BMAR)  
FY 1993 - 1997

- Scarce resources must be allocated to the Army infrastructure to ensure safe, high-quality facilities for its soldiers.
- The Army will be a good neighbor to its civilian communities and will abide by Federal, state, and local environmental regulations.
- Deferring routine maintenance to fund more urgent requirements may result in greater outlays in future years.
- Force structure changes are placing additional strains on the existing installations.



Fiscal Year	FY 93	FY 94	FY 95	FY 96	FY 97
OCONUS*	1,583	1,693	2,495	2,916	3,361
CONUS	1,150	1,699	2,082	2,582	3,131

Excludes Medical Facility Support

\* Outside Continental United States (OCONUS)  
Continental United States (CONUS)

***The Backlog of Maintenance and Repair is increasing as routine maintenance is deferred.***

Barracks Renewal Program, that focus the limited military construction budget on ensuring that all CONUS barracks meet new Army standards within 40 years. However, the programs are inadequately funded.

***Maintaining a high quality of life for the Army's soldiers is imperative to maintaining readiness.***

The Backlog of Maintenance and Repair (BMAR), a measure of existing maintenance and repair needs for the Army's facilities, has increased over the past seven years and is expected to continue to increase. As funding is diverted from installation support to contingency operations, the cost of future repairs increases as a result not only of the backlog, but also of the extent of repairs required, because preventive maintenance is bypassed or deferred. Eventually, repair becomes uneconomical and facilities must be replaced, at a much higher cost.